Preface

In 1961, Pres. John F. Kennedy proposed substantial cuts in personal and corporate taxes. When a reporter asked why, he replied:

> “To stimulate the economy. Don't you remember your Economics 101?”

Unfortunately, that quote has become a poison pill and Americans swallowed it hard.

Most economists believe that tax cuts can temporarily provide a temporary stimulus to the economy in times of recession, but they also know that the living standards of future generations depend heavily on the rate at which an economy saves for investment in future productive capacity.

Empirical evidence has shown that certain forms of taxation discourage saving, but incessant tax cutting has created large budget deficits that have reduced gross saving from 21 percent of gross national income in 1961 (when Kennedy made his remark) to 14 percent in 2004.

Kennedy is not responsible for this sad state of affairs however. Economists are.

In contrast to the modeling process that students learn when they study the business cycle, most introductory textbooks relegate economic growth to two dozen pages of text. A person who only took the introductory course, simply does not remember those vague pages on the determinants of output per worker as well as he remembers the results that he had to derive algebraically.

It's no surprise therefore that many Americans believe that tax cuts are the cure for every economic ailment and it's no surprise that politicians unfurl the tax cut banner at the first opportunity. After all, tax cuts are the faith that economists have taught them.

Our fear of rigorously teaching growth theory has left a generation of students with a fundamentally flawed understanding of macroeconomic policy. As a result, the average American fails to see how incessant tax-cutting reduces the national saving rate and deprives his children of a better standard of living.

These *Lecture Notes* represent a first attempt to repair the damage. In writing these *Lecture Notes*, I have placed an extraordinary emphasis on long-run economic growth, so that students complete the course with a firm understanding of the politically unappealing choice that policymakers face between stimulating the economy in the short-run and laying the foundation for long-run growth through increased saving.

In writing these *Lecture Notes*, I have followed the framework of N. Gregory Mankiw by first describing the goods, money and labor markets in the long run and then discussing how these markets may deviate from long run equilibrium over short periods of time when prices are not completely flexible.

A wonderful feature of Mankiw's framework is how it has enabled me to provide microeconomic foundation to the models of the economy in the short run.

Finally, I have not shied away from using mathematics in developing the models, but where I use math, I also provide intuitive explanations of the mathematical assumptions and results. I hope this will enable students to see how powerful a tool mathematics can be.

Knowledge of mathematics will become increasingly more important as computer technology makes increasingly more data available to us in the coming years. Students may dislike studying math today, but in the long run, they'll be better off … and that's the theme of this whole course.